CV Capital Pty Ltd

26 July 2023

SHAREHOLDER REPORT AS AT 30 June 2023

To my fellow shareholders & partners,

Financially speaking, FY2023 (1 July 22 to 30 June 23) has been quite an interesting year. It started with run-away inflation and the RBA responding with hiking interest rates at record pace. The prevailing narrative is that these rate hikes would further dampen demand from consumers already stretched by high inflation and a slowing job market that would tip the economy into recession. This recession, if it happens would be the most anticipated recession I can think of.

The market fell by 9% in the first quarter of the year but then staged a 6.4% recovery since hitting its lows in March. This is despite the RBA continuing to increase interest rates by 25 basis points each time in May and June (post the market lows) and confirmation that both consumer spending and economic growth are indeed slowing.

One would think that if the market was concerned about interest rates putting the economy into a recession, the market would go lower as interest rates increased. The problem with this thinking is that it doesn't consider the expectations of the market participants (i.e. what is priced into the market). An important lesson in investing is that excess returns are made in the gap between expectation and reality.

Markets often overshoot on the upside and the downside (creating boom and bust cycles), so a stock with an encouraging future (e.g. AI) tends to be priced to perfection and on the flip side a stock with issues (e.g. Chinese banks) tends to be priced for a terrible outcome. The reasons for this are mostly human psychology; herd mentality, loss aversion, confirmation bias etc.

Fund Activity

We regretfully sold our entire position in Boustead Project (AVM). Parent company Boustead Singapore (F9D) launched a takeover offer for Boustead Projects in February 2023 for the shares it did not already own. We begrudgingly accepted the offer price of S$0.95 which was far below the independent expert's fair value assessment of the net asset per share value of $1.85. F9D already owned 75% of AVM's share capital prior to launching the takeover offer and they were very likely to get to a 90% compulsory offer position so I thought why delay the inevitable.

We own F9D as well so I took circa 40% of the sale proceeds and increased our position in F9D given F9D was getting such a fantastic deal (paying $0.95 but getting $1.85). Overall, we made 36% on AVM over a 3 year holding period. This transaction has slightly tainted my impression of F9D's management because even though S$0.95 represented circa 14% premium above the market price of AVM's shares, I think F9D should have done the honorable thing and offered a fairer price for the shares (perhaps closer to the net asset book value of S$1.31).

We continued to purchase more shares in Baby Bunting (BBN) as the share price continued its falls. Compared to 1 July 2022, we have now increased our position in BBN by over 200%. Based on market values, our portfolio weighting in BBN is currently 13.7%. I'm happy with this current weighting as it gives us good upside potential when things recover and we're unlikely to add significantly to this position assuming no change in fundamentals and price. Please refer to previous reports (March 2023) for my rationale for purchasing more BBN shares.

Fund Performance

All the return figures quoted below will be corroborated by our accountant once the FY2023 financial statement is finalised. Relative to our benchmark, our FY2023 performance has been the most disappointing to date. CV Capital's return for FY2023 (1 July 22 – 30 June 23) is minus 0.9% (including FY22 dividends and after FY22 performance fees). Over the same period, our benchmark's (STW) return was 18% resulting in a 19% underperformance.

The FY2023 underperformance was primarily driven by a fall in BBN, which fell by 66% between 1 July 2022 and 30 June 2023. At the start of the year, BBN had a 12.3% weighting in our portfolio and we have been buying on the way down so the majority of our recent purchases are in an unrealised loss position. A key reason why the portfolio's return was not worse than reported is because our arbitrage trades made realised gains of circa 10% in FY2023 which offset the bulk of BBN's losses. I'm hopeful that FY2023 marks our low point because we have a few positions such as Donaco International (DNA) and Academies Australasia Group (AKG) which I expect to do well over the next 12 months as their Covid recoveries accelerate. Gambling revenue has been steadily improving in DNA's casinos in Cambodia and Vietnam but its share price has not moved much from its Covid lows. AKG's recovery is also set to continue in-line with the recovery in international students back to pre-covid levels.

Our poor performance in FY2023 means that no performance fees will be paid this year. On top of that, your manager will need to make up the 19% shortfall to our benchmark in FY23 before a performance fee can be paid in FY2024.

Since inception our returns are 9.7% (before performance fees) and 9.0% (after performance fees) on an annual compounded basis.

Subject to our accountant's corroboration, the share price as at 30 June 23 is $1.21. Details as follows:

Indicative values	Per share
Securities portfolio value	$1.15
Cash	$0.06
Franking credits	$0.04
Share price	**$1.25**
Less: Unpaid tax on realised gains	($0.04)
Subscription price	**$1.21**

Over the next few weeks, our accountant will finalise our financial statements and we will declare a dividend for FY2023. Given the sole purpose of our dividend payment is to release our franking credits to our shareholders, I encourage all holders to reinvest the FY2023 dividend. Please let me know as soon as possible if you choose not to do so.

YOURS SINCERELY,
DARRELL CHEAH